United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF FOR REHEARING EN BANC

75-7608

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IN THE

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FOR THE SECOND CIRCUIT

Docket No. 75-7608

IRVING SANDERS, *Plaintiff-Appellee,*

—against—

LEON LEVY, *et al., Defendants-Appellants.*

EGON TAUSSIG, *Plaintiff-Appellee,*

—against—

SIDNEY M. ROBBINS, *et al., Defendants-Appellants.*

MICHAEL SHAEV and RITA SHAEV, *Plaintiffs-Appellees,*

—against—

ERIC HAUSER, *et al., Defendants-Appellants.*

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

REPLY BRIEF FOR DEFENDANT-APPELLANT OPPENHEIMER FUND, INC. ON REHEARING EN BANC

WEISMAN, CELLER, SPETT, MODLIN,
WERTHEIMER & SCHLESINGER
Attorneys for Defendant-Appellant
Oppenheimer Fund, Inc.
425 Park Avenue
New York, New York 10022

Of Counsel
MILTON C. WEISMAN
GERALD GORDON

17

INDEX

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POINT I

THE COST OF IDENTIFYING MEMBERS OF THE CLASS IS PART OF THE COST OF NOTICE IMPOSED ON PLAINTIFFS

The format of Plaintiffs' argument in this Court en banc is:

1. The discovery rules are applicable to the identification of class members;

2. The District Court had discretion to impose the cost of culling out the names of class members on Oppenheimer Fund, Inc. (the "Fund") and its ruling was not an abuse of discretion; and

3. If the costs of culling the names is regarded as a notice cost, the District Court had discretion to impose the cost on the Fund.

Plaintiffs' argument puts the cart before the horse and is based on a house of cards that must tumble when confronted with precedent, logic and Rule 23(c)(2) of the Federal Rules of Civil Procedure ("FRCP"). In the first instance, this appeal arises out of plaintiffs' motion for class action determination and their obligation to give individual notice to all members of the class who can be identified through reasonable effort. The plaintiffs ignore reality until page 45 of their brief when they admit,

although overstate the issue, that the "inevitable approach urged by the defendants herein, and taken by the majority, is the creation of a hard-and-fast rule that the plaintiff in a class action must pay the cost of notice, irrespective of legitimate considerations like those in the instant case." The fatal flaw in the foregoing statement is the claim that there are legitimate considerations in this case, the kind of unsupported bootstrapping used by plaintiffs, similar to the bootstrapping used by plaintiffs in contending at length, ad nauseum, and in error as hereinafter discussed that the defendants here have expanded the size of the class and thereby caused an increase in the expense of notifying members of the class. (e.g., plaintiffs brief, pages 32, 33, 41, 42, 45, 52 and 53).

In Eisen v. Carlisle & Jacquelin, 417 U.S. 156 (1974) ("Eisen IV") the Supreme Court reviewed the history of the notice provision under FRCP Rule 23(c)(2) as well as the unmistakeable import of the Rule that "individual notice must be sent to all class members whose names and addresses may be ascertained through reasonable effort." 417 U.S. at 173. The Supreme Court noted that Mr. Eisen had argued that the prohibitively high cost of providing individual notice to 2,250,000 class members would end his suit as a class action and thereby frustrate his attempt to "vindicate the policies underlying the antitrust and

securities laws". Id at 175-76. This argument, which has been also set forth in plaintiffs brief, page 37, was rejected by the Supreme Court which clearly and unequivocally stated that "individual notice to identifiable class members is not a discretionary consideration to be waived in a particular case. It is, rather, an unambiguous requirement of Rule 23". Id at 176. (emphasis added) Indeed, the Supreme Court went further and stated that "[t]here is nothing in Rule 23 to suggest that the notice requirements can be tailored" to fit the pocketbook of particular plaintiffs." Id at 176. There was not even a hint by the Supreme Court that the discovery rules determined who must bear the cost under such circumstances.

Faced with the majority's ruling that the cost of culling out the names of members of the class is a Rule 23(c)(2) issue, the plaintiffs then argue that the "usual rule" requiring plaintiffs to bear the cost of notice has a built-in broad exceptionary base and that the district court may properly exercise discretion. (plaintiffs brief, page 39) We submit that just like Judge Tyler had no discretion to conduct a mini-hearing in the Eisen litigation to assess 90% of the cost of notice on defendants because Mr. Eisen was "more than likely" to prevail, Judge Griesa had no discretion here to impose the cost on the Fund because of an obviously lesser standard that the Fund had

fiduciary duties to plaintiffs, especially where no breach has been admitted and indeed has been vigorously opposed in these adversarial proceedings. Indeed, that was not the articulated standard justifying Judge Griesa's decision; it was the Fund's ability to pay the "modest" cost of $16,580 (an amount comparable to the $21,720 Mr. Eisen did not want to pay to litigate his action involving an individual stake of $70.) Here, plaintiffs' average stake is $12.24 and they, like Mr. Eisen, do not want to properly finance their notice requirements. They would rather "tailor" such requirements to their benefit and to the detriment of the Fund and all of its shareholders.

In arguing that the identification costs are governed by the discovery rules, plaintiffs raise emotional issues with respect to the need to prosecute class actions (plaintiffs brief, pages 36-38), the type of argument which this Court cautioned must be rejected when procedural safeguards for the benefit of all litigants must be followed. Eisen v. Carlisle & Jacquelin, 479 Fed. 1005, 1013 (2d Cir. 1973), ("Eisen III"), vacated and remanded, 417 U.S. 156 (1974). This warning, pointed out by the Fund on pages 24-25 of its initial brief before this Court, en banc, and by the American College of Trial Lawyers as Amicus Curiae, (the "College") at pages 4-5 of its brief, obviously is not understood or appreciated by plaintiffs who claim they find the College's constitutional argument with respect

to confiscation "difficult to understand" and then cavalierly reject it without any authority. The College's well reasoned point on this issue is not really difficult to perceive. If a defendant in a criminal case is presumed to be innocent until proven guilty, then a defendant in a civil case should not prior to jury verdict or court decision after trial bear the cost of financing the civil case against it because it had a fiduciary duty which it allegedly breached. We submit that just like the mini-hearing was deemed improper by Eisen III and Eisen IV, an exception based solely on "fiduciary duty" would constitute "legalized blackmail". See Eisen III, 479 F.2d at 1019.

It is stated by plaintiffs that the College has not cited any authority in support of the "novel proposition" that the plaintiffs should post a bond to secure the payment of expenses imposed on the Fund by the District Court. Indeed, plaintiffs state this would be contrary to accepted practice. However, the Fund previously cited such authority on page 27 of it's initial brief before the panel, i.e., Berse v. Berman, 60 F.R.D. 414, 416 (S.D.N.Y. 1973). See also Herbst v. International Telephone and Telegraph Corporation, 495 F.2d. 1308, 1324 (2nd Cir. 1974) where the plaintiff had refused to post such a bond. Furthermore, the Fund had on reargument of the District Judge's decision of May 30, 1975 asked the District

Court to impose such requirements on plaintiffs.[1] In Berland v. Mack, 48 F.R.D. 121, 132 (S.D.N.Y. 1969), a pre-Eisen III case, Judge Mansfield considered the possibility of allocating the costs in part on a corporate defendant and stated:

> "Where the claim appears to be a meritorious one and defendants desire it be prosecuted through a class action, it does not seem unreasonable to require the corporate defendant to share the cost of notice, particularly in a case where plaintiffs may be able to reimburse the corporation if the claim is dismissed. On the other hand, where the claim's merit is doubtful, the cost of notice is high, the defendants have no particular desire to gain the advantages of class res judicata, and plaintiffs would be unable in the event of dismissal to reimburse the corporation, plaintiffs should be required to pay out the initial expense rather than obtain a "free ride" at the corporation's expense. The mere fact that Rule 23 was enacted to facilitate the prosecution of class actions in cases where fraud is claimed does not dictate a policy in favor of using corporate funds as a means of financing essential expenses involved in such lawsuits. To the extent that class actions are to be encouraged as a means of private enforcement of federal securities laws, the more appropriate way of funding expenses in such suits would be through public appropriation rather than by a court order forcing an unwilling corporate defendant to pay the expense of plaintiffs prosecuting against it suits which may eventually be dismissed."

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[1] See Page 7, Memorandum in Support of Defendant Oppenheimer Fund, Inc's Motion for Reargument, Index to the Record on Appeal, 69 Civ. 1242, Document 106.

There are some offhand comments, made by plaintiffs in footnotes, which cannot be ignored. For example on page 46 of their brief, after seven years of litigation in which no damages were sought by them from the Fund, plaintiffs state their complaint does allege a breach of fiduciary duty by the Fund, obviously to help buttress their argument that the Fund is a "party" to the class action. We can only surmise that the "class champion" here has not sought damages from the Fund because that interest would have been antagonistic to the interests they purport to represent in their representative capacity on behalf of the Fund on their derivative claim. See e.g., Ruggiero v. American Bioculture, Inc. 56 F.R.D. 93 (S.D.N.Y. 1972).

On page 47 of their brief, plaintiffs make the outrageous statement that it is interesting to note "the directors of the Fund and the Manager, . . . have compelled the use of the Fund's assets to contest claims in this class action". The Fund is a party in this complaint because plaintiffs here named it as a defendant; it has not been brought in as a third party defendant by the other defendants. The Fund will obviously receive requests for indemnification for expenses incurred by its directors to the extent permitted by the New York Business Corporation Law - expenses generated by the plaintiffs in bringing their actions. Furthermore,

having been made a party herein, the Fund owes a duty to all of its shareholders not to waste its assets by paying the cost of notice required of plaintiffs. As noted by Judge Mansfield in Berland v. Mack, supra, "we doubt that most stockholders expressly or impliedly consent to such a use of corporate funds for vindication of an issue as to fiduciary duty merely because it is raised by one of them". 48 F.R.D. at 132. The College correctly points out that requiring the Fund to lay out such costs without protection would amount to confiscation.

A blatant example of plaintiffs' intransigence is exemplified by the footnote at pages 36-37 of their brief where they deny stating that defendants cannot be reimbursed for the costs if they prevail. This in the face of (1) their repeated statements throughout this matter that if plaintiffs are required to pay such costs they will not proceed with the action and (2) that the average plaintiffs' claim is $12.24 and such costs are approximately $16,580.00 (based upon 1973 estimates). Instead of frankly and in fairness to this Court admitting this obvious fact they resort to the "non-sequitur" of urging that this is a matter of taxation of costs. We submit that such lack of candor demonstrates that this case does not require any exception to the usual rule that plaintiffs must bear the cost of notice.

POINT II

THE DISCOVERY RULES ARE NOT APPLICABLE TO INDENTIFICATION OF MEMBERS OF THE CLASS.

We respectfully submit that we have heretofore demonstrated that determining the identity of class members is governed by FRCP Rule 23(c)(2), not by the discovery rules. While identity does in effect require discovery, the legal principles applicable to the costs of discovery are not determinative in such instance.

We believe the majority of the panel, the other defendants and the College have correctly distinguished between discovery of information relating to the identity of class members and discovery needed in assisting plaintiffs in meeting their burden of showing that elements of a class action are present. The drawn out discussion by plaintiffs' counsel on pages 21-28 of their brief does not refute the validity of our argument to such effect and their conclusion that such argument is "wholly unfounded" (plaintiffs brief, page 27) and that no distinction exists (Id., page 28) is of itself without any support and is founded upon their "ipse dixit" alone.

Plaintiffs seek comfort for their position in the claim that the defendants did not object to discovery herein with respect to how to indentify class members (Id., at pages 9, 26) and from this urge that this in effect justifies discovery of such names under the discovery rules.

The foregoing disregards the fact that in the first instance as admitted by plaintiffs on page 9 of their brief, defendants did object to the form of discovery because of the expenses generated thereby. Counsel for plaintiffs argued at such time that under Eisen II, parties were entitled to limited discovery relating to the notice issue and Judge Griesa said that he would "permit some discovery but not extensive".[2] Defendants never conceded that the discovery rules applied; they did submit briefs to the District Court which argued that the costs must be borne by plaintiffs if the discovery rules were applicable. In any event, the District Judge's opinion was silent in this respect.

Furthermore, as heretofore mentioned, whether the cost of identification is governed by FRCP Rule 23(c)(2) or by the discovery rules, there is no basis for plaintiffs' argument that defendants have caused an increase in such costs. The plaintiffs' dilemma arises from (1) their three year delay from April 24, 1970 in making the class action motion during which period the Fund must have acquired new shareholders and lost existing shareholders and (2) the correct rejection of plaintiffs' proposal to minimize costs by improper notification procedures. Plaintiffs

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[2] See page 36, Transcript of Record of Proceedings, May 23, 1973, Index to the Record on Appeal, 69 Civil 1242, Document 70.

defined the class, i.e., all purchasers of Fund shares from March 28, 1968 to April 24, 1970, and defendants' efforts to have the class virtually cut in half and limited to purchasers in the March 28, 1968 to April 25, 1969 period were vigorously opposed by plaintiffs and rejected by the District Court (A-176-177).[3] During the pendency of the class action motion, it was plaintiffs who, realizing that the notice costs exceeded their willingness (and probably ability) to pay, desired to eliminate former shareholders from members of the class. Plaintiffs fail to realize or point out that the costs would not be substantially decreased if such shareholders were eliminated from the class because the keypunch operators who input the names of purchasers would have to first identify these persons in any event and then remove them from the computer list created by the program after checking shareholder names from current shareholder tapes.

Plaintiffs further erroneously urge that the increased costs arise because their proposal to mail notice to all shareholders of the Fund was opposed by defendants. They completely disregard the fact that the District Judge ruled that the notice should not be sent to non-members of the class (A-178) and the majority of the panel agreed that the defendants

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[3] Reference is to pages of the Joint Appendix.

had a legitimate concern as to the possible prejudicial impact on the Fund if a mass mailing of notice was made to all Fund shareholders. As we pointed out in our original brief before the panel (page 19) there are serious problems caused by establishing a precedent of mailing class notice to all shareholders of a defendant issuer, whether or not members of a class. Where the corporation is an investment company, the mass mailing might result in panic among shareholders who would redeem their shares, much akin to a "run on the bank" by nervous depositors having heard of alleged financial difficulties of the bank. Other corporations might find that their shareholders would sell shares on the open market, driving down the market price of shares. In either instance, all the shareholders of the corporation, whether or not members of the defined class, could be harmed because a "class champion" sought to reduce his notice expense - and to the detriment of both class members and non-members. As a general rule and upon the facts of this case, particularly the small size of the average claim ($12.24), such attempt must be rejected both for its prejudicial effect and its non-compliance with FRCP Rule 23(c)(2). It also avoids possible manageability problems or solicitation problems as pointed out in our original brief before the panel (page 18).

CONCLUSION

For the reasons stated, we respectfully submit that the result reached by the majority of the panel reversing the order of the District Court with respect to the allocation of identification costs was correct and that such decision should stand as the holding of this Court en banc.

Respectfully submitted,

WEISMAN, CELLER, SPETT, MODLIN,
WERTHEIMER & SCHLESINGER
Attorneys for Defendant-Appellant,
Oppenheimer Fund, Inc.
425 Park Avenue
New York, New York 10022
(212) 371-5400

MILTON C. WEISMAN
GERALD GORDON
of Counsel

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CERTIFICATION OF SERVICE

I, GERALD GORDON, an attorney admitted to practice in this Circuit, do hereby certify that, on this 22nd day of October, 1976, two copies of the Reply Brief on Rehearing En Banc for Defendant-Appellant Oppenheimer Fund, Inc. were hand-delivered to the following enumerated counsel at their respective addresses:

WOLF POPPER ROSS WOLF & JONES
Attorneys for Plaintiffs-Appellees
845 Third Avenue
New York, New York 10022

GUGGENHEIMER & UNTERMYER
Attorneys for Oppenheimer Management Corp., Oppenheimer & Co., Leon Levy and Jack Nash, Defendants-Appellants
80 Pine Street
New York, New York 10002

THACHER PROFFITT & WOOD
Attorneys for Defendants-Appellants, Edmund T. Delaney and Emanuel Celler
40 Wall Street

DEBEVOISE, PLIMPTON, LYON & GATES
Attorneys for the American College of Trial Lawyers
299 Park Avenue
New York, New York 10017

Gerald Gordon